N O T E S O N

DEBTOR/CREDITOR

R E L A T I O N S

October 2017

Failure to Inform as Fraud

An attorney who failed to file a malpractice suit against another attorney before the statute of limitations had expired gave his client a promissory note in the amount of $275,000 in exchange for her agreement not to file a disciplinary complaint or a malpractice action against him. The attorney did not make any payments on the note. When the former client sued on the note, the attorney filed a Chapter 7 bankruptcy case.

The federal appeals court in New Orleans affirmed the decision of the bankruptcy judge that the attorney's obligation on the note could not be discharged due to actual fraud. The Louisiana rules of professional conduct required the attorney to advise his client in writing of the desirability of seeking independent legal counsel in connection with the client's malpractice claim. The court held that failure to give this advice rendered the promissory note a false representation for purposes of the bankruptcy law.
Selenberg v. Bates (In re Selenberg), 856 F.3d 393 (5th Cir. 2017).

Affirmative Act Required to Violate Stay

The automatic stay of the bankruptcy statute prohibits "any act… to exercise control over property of the estate." The majority of appellate courts have ruled that a secured creditor passively holding collateral that it has repossessed from the debtor "exercises control" and violates the bankruptcy stay. The practical effect of this ruling requires a secured creditor to return the repossessed collateral to the defaulting debtor, even without an order of the court.

A federal appeals court in Denver recently took the minority position and held that no stay violation occurs unless the creditor takes some affirmative act after commencement of the bankruptcy case. The creditor is not required to return the collateral to avoid a stay violation.

Notwithstanding this decision, a creditor that has repossessed and is holding collateral is best advised to immediately seek permission from the bankruptcy court to continue holding the collateral.
WD Equipment, LLC v. Cowen (In re Cowen), 849 F.3d 943 (10th Cir. 2017).

Bankruptcy Sale Cleans Toxic Assets

RG Steel sold the Sparrows Point steel mill pursuant to an order of the bankruptcy court approving the sale free and clear of liabilities for environmental contamination. Subsequently, the owner of the adjoining property sued the purchaser under the Comprehensive Environmental Responsibility, Compensation and Liability Act for toxic chemicals that had migrated from Sparrows Point to the adjoining property.

A federal court in Baltimore determined that the bankruptcy court's approval of the purchase protected the purchaser from CERCLA liability for the environmental contamination.
SPS L.P. LLLP v. Sparrows Point, LLC, 2017 U.S. Dist. LEXIS 144740 (D. Md. 2017).

○ ○ ○

This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation. Congress has required bankruptcy attorneys to state: "I am a debt relief agency. I help people file for bankruptcy relief under the Bankruptcy Code." 11 U.S.C. § 528. If you wish to receive "Notes on Debtor/Creditor Relations", go to www.jamesolsonattorney.com/newsletter.html and click on the link at the word "here".

Prepared by James C. Olson, Attorney and Counselor at Law

One Corporate Center Suite 400 10451 Mill Run Circle Owings Mills, MD 21117 410-356-8852 Fax 410-356-8804 jolson@jamesolsonattorney.com